

## **Commentary: Use caution with worker job classifications**

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Long Island, NY - Despite recent news that the economy may have bottomed out, businesses large and small continue to look for ways to cut costs. One method: Retain independent contractors in lieu of employees and reclassify current employees as independent contractors. For example, a recent SurePayroll Contractor Index says small businesses' use of independent contractors reached a record because of the current economic climate.

But this strategy can land companies in hot water. Individuals or classes of individuals often are improperly classified as independent contractors, leading to abuses of the federal and state governments, as well as the individuals. In fact, according to recent IRS data, employers have misclassified more than 3 million workers.

From the government's view, misclassification results in unpaid federal, state and local tax withholding, as well as unpaid Social Security and Medicare contributions. By misclassifying an individual, companies also avoid paying unemployment insurance and workers' compensation premiums. For workers, misclassification means they will be excluded from coverage from virtually all anti-discrimination and wage/hour laws, resulting in the potential loss of monetary relief and benefits.

Recent initiatives from all government branches highlight the need for proactive compliance.

Currently, federal and state agencies are stepping up efforts to audit companies and recoup (with penalties and fines) the monetary losses sustained because of misclassification. This year alone, the New York State Joint Enforcement Task Force on Employee Misclassification charged two contractors with criminal penalties arising out of fraudulently misclassifying employees as independent contractors to evade unemployment insurance fund obligations.

Legislatures also have sharpened their focus on this issue. More than a dozen states have enacted or proposed legislation setting rules for classifying independent contractors in certain industries and providing for steep financial penalties for noncompliance. On July 30, Rep. Jim McDermott, D-Wash., introduced federal legislation to define classification rules. Finally, courts have addressed the issue in a number of industries, including transportation, brokerage and medical.

So, what should your business do? While you can never eliminate the possibility of a lawsuit or agency audit, there are ways you can minimize the potential for future liability:

- Understand the thumbnail factors to distinguish employees from independent contractors. For more information on IRS standards, visit [www.irs.gov/newsroom/article/0,,id=173423,00.html](http://www.irs.gov/newsroom/article/0,,id=173423,00.html).
- Conduct internal audits to ensure individuals (or classes of individuals) are properly classified as independent contractors. It is important to look not only at a job title or written position statement defining job duties, but also at the actual day-to-day functions being carried out by the individuals.
- Maintain a well-documented file setting forth the criteria relied upon by the company, and the reasons the workers are classified as independent contractors instead of as employees.
- Consider opting for a responsible third-party leasing organization to provide workers. In such cases, the workers will be deemed employees of the leasing organization, which in turn would withhold taxes, make the appropriate unemployment and workers' compensation payments, and also perhaps provide various other employee-like benefits.

Before you classify or hire a worker as an independent contractor, it is vital to ensure your cost-cutting strategy isn't going to cost your business.

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